

NOTICE OF INVESTIGATION AND TERMS OF REFERENCE

Investigation of Hydro Tasmania's pricing policies in the provision of raise contingency frequency control ancillary services to meet the Tasmanian local requirement

Background

Regulation 23 of the *Electricity Supply Industry (Price Control Regulations) 2003* requires the Regulator to conduct an investigation into the pricing policies of an electricity entity in respect of a declared electrical service. This investigation follows the Regulator's decision to declare certain services provided by Hydro Tasmania as declared electrical services. The background and reasons for that decision are contained in the Regulator's *Declaration of Frequency Control Ancillary Services - Statement of Reasons - December 2009*.

The Price Control Regulations establish the procedural framework to be followed by the Regulator in conducting pricing investigations.

Sub-regulation 24(1) requires that, before conducting a pricing investigation, the Regulator give notice of the investigation. Such a notice is to be provided in writing to the Minister and each electricity entity providing the declared electrical service that is the subject of the investigation. Notice is also required to be published in such daily Tasmanian newspapers as the Regulator considers appropriate.

This notice, containing the Terms of Reference for the investigation, is issued pursuant to regulation 24 of the Price Control Regulations.

Purpose of the pricing investigation and services to be investigated

The purpose of this investigation is to investigate and make a determination that regulates the prices that may be charged by, and specifies the price control mechanisms imposed on, Hydro Tasmania for the provision of the following declared electrical services:

- fast raise contingency frequency control ancillary service;
- slow raise contingency frequency control ancillary service; and
- delayed raise contingency frequency control ancillary service;

to meet the Tasmanian local requirement.

Matters to be considered

Regulation 33(2) of the Price Control Regulations contains a range of matters that must be considered by the Regulator in conducting price investigations:

- (a) the cost of providing the declared electrical service;
- (b) any interstate or international benchmarks for prices, costs, revenues and return on assets in bodies providing a service similar to the declared electrical service;
- (c) the principle that consumers of the declared electrical service should be protected from the adverse effects of the exercise of substantial market power by an electricity entity in relation to prices, pricing policies and standards of service in respect of the provision of the declared electrical service;

- (d) the degree of competition in the electricity supply industry that is relevant to the provision of the declared electrical service;
- (e) the principle that there is a need for a reasonable return (including the payment of dividends) on the assets of an electricity entity;
- (f) the principle that there is a need for efficiency in the provision of the declared electrical service for the purpose of benefiting the public interest through a reduction in the cost of providing the declared electrical service;
- (g) the effects of inflation;
- (h) the principle that there is a need for the electricity entity to be financially viable;
- (i) the impact on pricing policies of any borrowing, capital, dividend and taxation or tax equivalent obligations of the electricity entity, including obligations to renew or increase assets;
- (j) the quality of the provision of the declared electrical service
- (k) any ministerial charter, licence or obligation under the Act or the regulations that applies, or is likely to apply, to the electricity entity;
- (l) the Tasmanian Electricity Code;
- (m) any costs (including capital expenditure) incurred by the electricity entity at the direction of the Regulator; and
- (n) the public interest.

The Regulator may also consider any other matter that he considers to be relevant.

Prices and price control mechanisms

Regulation 18 specifies the manner and terms in which the prices and price control mechanisms may be expressed. These include, but are not limited to:

- (a) maximum prices or the maximum rate of increase or the minimum rate of decrease in maximum prices;
- (b) average prices or average rates of increase or decrease in average prices;
- (c) pricing policies or principles;
- (d) by reference to a general price index, the cost of production, revenue, a rate of return on assets or any other factor;
- (e) by reference to quantity, location or period of provision of the declared electrical service;
- (f) by reference to a maximum revenue;
- (g) any other terms the Regulator considers appropriate.

As part of the investigation, and prior to the publication of a Draft Report in respect of the investigation, the Regulator will consult on an appropriate price control mechanism to be imposed on Hydro Tasmania.

Price determination

After completing the Final Report in respect of the investigation, the Regulator will make a determination, pursuant to regulation 31 of the Price Control Regulations, that regulates the prices that may be charged by, and specifies the price control mechanisms imposed on, Hydro Tasmania in respect of the declared electrical services during the period specified in that determination.

Period for price determination

The Regulator has yet to determine the date on which a determination will commence and expire. The Regulator will consult stakeholders on this matter during the investigation.

Objective and principles

The Regulator's objectives in undertaking this investigation and making a determination are to promote efficiency and competition in the Tasmanian electricity supply industry and protect electricity consumers from the adverse effects of the exercise of substantial market power. In achieving this objective, the Regulator will apply the following principles:

1. The price control mechanism to be applied to the supply of the declared electrical services will:
 - (a) be consistent with the National Electricity Objective;
 - (b) not be unduly onerous on Hydro Tasmania in its application;
 - (c) have minimal impact, if any, on the wider National Electricity Market; and
 - (d) not require an amendment to the National Electricity Rules nor add complexity to the National Electricity Market dispatch process.
2. The price control mechanism to be imposed on, and the prices to be charged by, Hydro Tasmania will:
 - (a) be fair and reasonable;
 - (b) enable Hydro Tasmania to recover its costs for the efficient provision of the declared electrical services;
 - (c) provide market signals that promote efficiency and maximise incentives for other parties to supply raise contingency FCAS in the Tasmanian region; and
 - (d) not impose significant regulatory costs on the Regulator or Hydro Tasmania.

Date for completion of the investigation

The Regulator will complete the investigation by 26 November 2010 and publish the Final Report on that date.

Following completion of the Final Report, the Regulator will:

- provide a copy of the Final Report to:
 - the Minister for Energy;

- the Treasurer; and
- Hydro Tasmania, as the body providing the declared electrical services which is the subject of the investigation;
- publish the report on the OTTER website;
- notify in newspapers of the availability of the report; and
- make available copies of the Final Report to relevant stakeholders and members of the public on request.

Conduct of the investigation

The conduct of the investigation must include reasonable regulatory accountability through transparency and public disclosure of regulatory processes and the basis of regulatory decisions. The Regulator will do this through the publication of decisions and reasons for those decisions.

Submissions

Submissions will be sought on relevant matters contained in the Notice of Investigation and Terms of Reference, Hydro Tasmania's submission, any published consultants' reports and the Regulator's Draft Report. The Regulator will provide reasonable notice of the call for submissions in accordance with the Regulator's *Consultation Policy and Procedures of the Tasmanian Economic Regulator, Version 2, 2009*.

Submissions must be made in writing and may be lodged by email to office@economicregulator.tas.gov.au or by mail to OTTER at GPO Box 770, Hobart, Tasmania, 7001.

Submissions will be published on the OTTER website. If a person making a submission does not wish that submission, or a part or parts of it, to be placed on the website, the submission must indicate which part or parts are to be excluded. Confidential submissions will be treated in accordance with the Regulator's *Policy on the Treatment of Confidential Submissions*.

Draft Report

Pursuant to regulation 29 of the Price Control Regulations, at an appropriate time during the price investigation, the Regulator will make available a Draft Report and take public submissions in respect of the Draft Report.

Public hearings

Pursuant to regulation 25, the Regulator will conduct a public hearing in regard to the investigation.

Notification

Notification of the publication of reports relating to this investigation will be given on the *What's New* page of the OTTER website www.economicregulator.tas.gov.au. Interested parties may subscribe, through the *What's New* page, to receive automatically generated emails when notices are published on *What's New*. In addition, publication of the Final Report will be notified in the newspapers.

Process and timetable for the investigation

Notice of, and terms of reference for, the investigation	6 March 2010
Hydro Tasmania's submission to the investigation published	30 April 2010
Public submissions on the terms of reference and Hydro Tasmania's submission close	21 May 2010
Consultant's report recommending price control mechanisms to be applied to Hydro Tasmania's provision of the declared electrical services published	18 June 2010
Public submissions on consultant's report close	9 July 2010
Publication of investigation Draft Report	No later than 8 October 2010
Public hearing	Within one week of closing date for submissions
Closing date for submissions on Draft Report	Four weeks from date of publication of Draft Report
Investigation completed and investigation Final Report published	No later than 26 November 2010
Determination of prices to be charged by, and price mechanisms imposed on, Hydro Tasmania	No later than 24 December 2010
Commencement of Determination	Yet to be established